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BUREAU OF INTELLIGENCE & RESEARCH  
OFFICE OF ANALYSIS FOR EAST ASIA AND PACIFIC

CHINA LIGHTS

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I. CHINA: DENG PLANS, AGAIN, FOR A STABLE SUCCESSION (2/6/91)

Though limited by bouts of ill health and diminished political clout, Deng Xiaoping has spasmodically intervened in decision-making.

Succession arrangements remain unsettled, and Deng appears to be trying with some urgency to bolster Yang Shangkun's ability to guide the transition after Deng dies. But a smooth succession is unlikely.

Deng Xiaoping, now 86 and in obvious physical decline, remains the arbiter of China's most difficult political decisions.

China's political system requires such an arbiter, especially when leaders are as divided as they are now.

Leadership stability

Deng's principal goal is to assure a stable succession. Since June 1989 he has successfully argued against any top-level changes.

In an apparent shift in tactics, probably reflecting greater concern over his own health, Deng now seems determined to ensure that 83-year-old Yang succeeds him as de facto chief arbiter.

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Protecting reforms

Deng is also widely believed to have intervened before the December party plenum to rebuff hard-liner efforts to sanction a rollback of reforms in the forthcoming five-and ten-year plans.

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A low-profile foreign policy

Since the Tiananmen crackdown, Deng has used his influence to promote caution in foreign affairs, hoping to weather the storm of foreign criticism and regain China's international stature.

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Obstacles in Deng's path

Given age and poor health, Deng is unlikely to be able to sustain his efforts, leaving the way open to infighting and jockeying over personnel and policy. China faces myriad contentious issues, including top-level state and party personnel changes, balancing anti-inflationary and stimulatory economic policies, and responding to US pressure on proliferation, human rights, and trade.

Yang's task of readying himself to fill Deng's shoes as arbiter while also protecting Deng's program and succession choices will not be easy. Other party and army leaders, including Yang's peers in the "revolutionary second echelon," frequently express concern about his accretion of military and security powers: some press their own preferences for party chief and premier. Yang may be forced into political moves or deals that go against Deng's preferences even while Deng is still around--fraying the long-standing, close Deng-Yang relationship. (Chamrin/CClarke/NSilver) (SECRET/NOFORN/NOCONTRACT/ORCON/EXDIS)

II. PRC/TAIWAN: TWO-TRACK POLICY (1/28/91)

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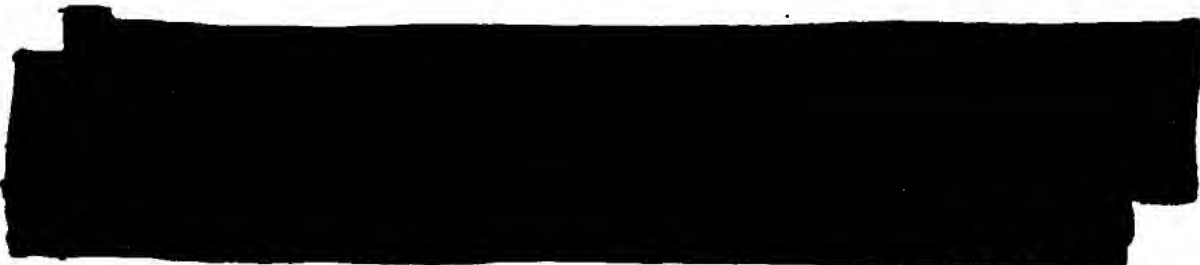
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### III. CHINA: BUDGET PROBLEMS HINT AT VICIOUS CIRCLE

Putting China's fiscal and monetary policies on sounder footings is in large part hostage to the stalemate in the leadership over economic reform and development policies for the 1990s and the struggle between Beijing and the provinces over budget resources. Excessive credit expansion last year makes another bout with inflation probable this year. The government is preparing a 1991 budget that reportedly will call for continued austerity, but it will be under pressure to help out struggling state enterprises. It hopes to muddle through by keeping the rise in the price level under 10%.

If economic growth remains sluggish, as expected, profits will continue to fall and losses mount at a growing number of state enterprises in most sectors and regions. The squeeze on revenue would worsen problems with the budget deficit and its financing, set the stage for more inflation, and further retard efforts to restructure industry and raise productivity.

#### Budget trends



China's state budget combines the central government budget with lower-level government budgets. Only in recent years has the finance ministry published a breakdown of budget line items according to level of government.

#### Revenue sharing

Because only the central government is authorized to issue debt instruments, its deficit is the one that counts in terms of financing requirements. The deficit for 1990 probably amounted to 26-27 billion yuan, 4%-8% over plan and about 1.5% of GNP. Most of the provinces do not directly collect enough revenue to cover expenditure and depend on transfers from the center to bridge the gap. The center in turn receives transfers from a few of the wealthier and more industrialized provinces, usually according to a contract that specifies the amount.

#### Thrust and counter

In the first half of the 1980s, the center enjoyed a net surplus from revenue transfers. The effects of fiscal reforms undertaken in the mid-1980s and subsequently, however, reversed

the flow and gave provinces a net surplus. Lower-level governments and enterprises have also become skilled at shielding sources of revenue from the center or moving them off budget. The center has countered with clawback measures--generally mandatory contributions to various funds, in effect surtaxes--that in 1990 accounted for 20% of central government revenue.

As a share of GNP, the center's budget has fallen sharply in recent years. The revenue squeeze and a sharp rise in subsidies to centrally operated enterprises have pinched centrally directed investment, while the share of investment undertaken by local government and enterprises has grown rapidly. Centrally placed caps on investment have held only temporarily. To regain control over economic development, the center is trying to raise its share of budget revenue, reduce subsidies, and shift more current expenditures and a greater share of the subsidy burden to local government. But the provinces are digging in their heels.

(INR/EC:WNewcomb) (SECRET/NOFORN/NOCONTRACT/ORCON)

IV. CHINA: PUZZLING APPOINTMENT IN GUANGDONG (2/4/91)

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V. TAIWAN: LEE TENG-HUI AT THE HELM

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